

BPR KB FINANCIAL PERFORMANCE IMPROVEMENT A SIMPLER APPROACH

Adi Prasetyo Raharjo, Deddy P. Koesrindartoto and Subiakto Sukarno
School of Business and Management
Institut Teknologi Bandung, Indonesia
adi.prasetyo@sbm-itb.ac.id

Abstract—*The bank in research is in a complicated situation where it is considered healthy by BI but under performing if being compared to other bank. Trough Du-Pont and common-size analysis, it is obtained that the bank in question is underleveraged and has lots of non-performing loan. And one way to increase the leverage is to analyze its funding product and provide a marketing plan accordingly. And creating an implementation plan and action plan to tackle the problem.*

Keywords: *Du-Pont, BPR, Common-Size, Business Model Generation*

I. INTRODUCTION

The business assignment was initially an external project to create a master plan for the purpose of increasing the amount of paid-in capital from the government. But upon the project, the author found some strangeness on the performance of the company and decided to find a way to improve it. The company is a Rural Bank owned by a regional government that is initially formed due to BI recommendation to merge all 15 banks owned by the regional government by Deputy Governor of Bank Indonesia Decision Number 11/15/Kep.DpG/2009 dated 15 December 2009. This merger is done to strengthen the capital of the rural bank in question.

As a rural bank, their main function is to provide fund to less bankable individual or company within their operational jurisdiction. While they are posed by a greater risk compared to conventional banking, but the interest they could charge is also greater to minimize the effect of the risk. The company seems to have a mediocre performance if it is compared to other rural bank. And if it is kept

this way, the BPR would lose its competitiveness, or even worse reputation as a bank. The Regional Government of Bandung Region also trying to pass a Regulation that state that the regional government companies should double its profit for every 3 years. The regulation itself becomes the business issue over which BPR Kabupaten Bandung is forced to review and restructure their business. This issue would be the business issue that will be explored in this final project.

The initial hypothesis is that the company's Assets and Liability Management is inefficient, therefore reducing the capability of profit making. So this analysis will improve the assets and liability management by creating an action plan.

II. BUSINESS ISSUE EXPLORATION

A. Conceptual Framework

In this framework, BPR KB will be analyzed from various sectors. First, its financial operation performance and the corresponding vision and mission. Both performance would be benchmarked with competitor performance, its compliance with BI Regulation and Regional Government Regulation.

Then the issue arise from the previous benchmark would be analyzed by proposing a hypothesis from the limited evidence as a starting point for a future investigation. Those hypotheses would be used to design an analysis and their source of information. At last, the process is followed by suggesting a rationale, which is a set of reason that serves as a logical basis for a course of action (in this case hypothesis). The rationale from all the issues would be used to propose a roadmap to overcome their issues. After a roadmap is established, each

section of the roadmap would be broken down into an action plan.

The parties which has prominent presence in this research are BI (the central Bank of Indonesia), the regional government, and the bank itself. BI as a regulator has a role to protect the public interest with the bank by setting up several regulation to keep the bank healthy, otherwise the bank would likely to fully chasing the profitability aspect of the business and might cause a liquidity, and solvability problem. This liquidity and solvability problem might lead to a bank rush and create a systemic crisis due to lack of trust to the bank.

According to (Indonesia, 2012a) Bank Indonesia as a Central Banking Institution have a single Objectives which is to obtain and then maintain the stability of Rupiah value. The goods and service value in Indonesia, and the value of foreign currency affect the value of Rupiah. The connection between Rupiah Value and Goods & Services Value are monitored by the rate of inflation, where the connection between Rupiah and Foreign Currency were monitored by the movement of foreign exchange rate to rupiah.

The other related party are the regional government of Bandung. As a legal entity in Indonesia that has been given autonomy right, the Regional Government is allowed to obtain additional source of revenue by creating a company, Regional Company Act UU No.5/1962 governs the creation of the company mentioned. This Company according to (Indonesia, 1962) is a productive entity who aims to serve general public and gathering additional revenue for the Regional Budget (APBD) needs. This company is created to help the government in the development of which they operate.

The equity needed for the creation of such company is being set aside from previous period Regional Budget according to the budgetary capability of a certain region. Let's take BPR KB as an example, the Regional Government through Regional Regulation Number 4/2009 stated that they will invest a sum of IDR 100,000,000,000.- at the Regional Budget Capability. The next year, Regional Regulation Number 3/2010 is enacted, this regulation grant IDR 10,000,000,000.- to BPR KB as Investment. The regional government still needs to invest another IDR 78,788,438,585. - (August 2011 Position) to meet the investment that they state on Regional Regulation Number 4/2009. The regional government also supervised the operation by appointing a board of supervisor

for regional company from a select of high-ranking official.

Bank Indonesia as a regulator recognizes the importance of soundness of a bank to its shareholder. Decision Letter of The Director of Bank Indonesia Number 30/12/KEP/DIR/1997 on Procedure of Determining the Soundness of Rural Credit Bank. The framework is simple enough to be applied and used for analysis. This framework has not been change and still sufficient for Rural Credit Bank, but the same cannot be said for Commercial Bank.

B. Method of Data Collection and Analysis

There are 2 (two) main sources of primary financial data that is the company's internal financial condition and a publicly available BI "Bank's Financial Report" which was then used to check the company. The two steps to analyze a bank's financial performance is to first determine whether it is healthy (according to regulation) or not. This research employ two approach of checking the rural bank's soundness.

The first method is to follow the procedure of scoring available on Director Decision Letter no 30/12/KEP/DIR/1997 of Bank Indonesia, which resulted on "healthy" verdict. While this is enough for a rural bank, the author is curious how is the rural bank in question perform if it is faced with a more stringent regulation with the framework provided by (Indonesia, 2004a) under (Indonesia, 2004b) as legal framework. Under this analysis a great performance would be rewarded with "1" score and "5" represent a poor performance. The bank shifted to the middle range of the performance.

Unfortunately being healthy is not enough for the bank to grow and prosper; they need to be on their top condition and doing the best practices available to ensure the company runs prudent, profitable and efficiently.

There has been proof that a Rural Credit Bank could grow to be a bank with assets of over trillion IDR, which is true for several Rural Credit Bank in Indonesia. The reason they succeeded is need to be analyzed, and would be dissected further in the next section of this final project.

Right after the bank were pronounced "healthy" by rural bank standards, the author continues the analysis by benchmarking the big picture (company vs company) by doing a Du-Pont analysis and Cross Section analysis. The

competitor selected for this analysis is BPR Karyajatnika Sadaya (BPR KS), Eka Bumi Artha (BPR EBA), Sri Artha Lestari (BPR SAL), Jawa Timur (BPR JT), Gunadhana Mitrasembada (BPR GM). Shows that BPR Sri Artha Lestari(SAL) and BPR Eka Bumi Artha (EBA)have the Highest ROE, followed by BPR Mitra Kanaka Sentosa (MKS), and BPR Karyajatnika Sadaya (KS).BPR Jawa Timur (JT), BPR Jelita Artha (JA) in the low digit range, and BPR Gunadhana Mitrasembada (GM)stand out as still making loss.Though the monthly ROE of BPR Gunadhana Mitrasembada is significantly positive, but the losses from previous year still haunt the company financial condition.

TABLE I. RESULT OF DU-POINT

DuPont Analysis September 2011	ROE (Year)	ROA (Year)	ROA (Year)	LM (Year)	GM	NM	REC
BPR KAB Bandung	24.07%	15.56%	3.28%	3.33%	4.56	4.81	100.21%
BPR Gunadhana Mitrasembada	-1.32%	43.82%	-0.08%	2.63%	16.55	16.65	54.66%
BPR Jelita Artha	11.23%	14.87%	3.75%	4.92%	2.98	3.03	81.36%
BPR Mitra Kanaka Sentosa	32.04%	29.35%	8.67%	8.79%	3.10	3.24	79.89%
BPR Karyajatnika Sadaya	27.62%	17.57%	2.24%	3.33%	12.33	11.49	68.48%
BPR Eka Bumi Artha	46.13%	30.23%	6.64%	4.97	4.69	65.34%	15.84%
BPR Sri Artha Lestari	71.92%	44.59%	4.01%	2.48%	17.94	17.82	46.96%
BPR Jawa Timur	15.21%	11.17%	2.70%	1.89%	5.63	6.03	72.67%

A breakdown of ROE into ROA and Leverage Multiplier (LM) providing further insight as how that ROE has been achieved with respect to genuine profitability of the asset base. Though BPR SAL and EBA have the two highest ROE, the way they approach their respective ROE is entirely different. While EBA has ROA two times bigger than SAL, but SAL compensate by having more than 3 times LM compared to those of EBA. Having this said, the other BPR rest in the middle of the ROA and LM.

The difference between Gross Margin (GM) and the Net Margin (NM) in BPR EBA is low which is signifying a more cost efficient structure compared to BPR SAL. While the higher LM in BPR SAL shows that the third party funds is plentiful compared to those of the competitor. LM serves as an amplifier of the financial condition, just like SAL who could gain more ROE than EBA due to the positive amplification effects; it could have a significant negative effect like what happen in BPR GM. Though it is a simple to use ratio, (Lim, 2010) remind that the LM is not a clear cut indication of inherently higher balance sheet risk. There is no appreciation of risk weighting attributed to the different assets on the balance sheet.

Though DuPont Formula Analysis is an excellent way to disaggregate the ROE of a company into its constituent parts. However, in the case of banks the methodology does not encompass analysis of capital adequacy, liquidity, or asset quality. Therefore, a supplement for DuPont Formula Analysis is needed as shown by Table 2. The banking ratio such as NPL, CAR, and LDR is regulated by Bank Indonesia and shown in the different colors representing their compliance.

Efficiency and OEOI is a measure of banking efficiency from the standpoint of income statement. Both of this ratio shows that a company with good efficiency ratio would have a high ROA,BPR EBA and BPR MKS shows a good example of this condition.The Non Interest Expenses to Total Assets (NIETA)shows the basic measure of efficient use of overhead, BPR EBA and SAL pass with flying colors. While BPR Kabupaten Bandung (KB) sadly have the highest overhead cost.

TABLE II. SUPPLEMENT FOR DU-PONT ANALYSIS

DuPont Analysis September 2011	Efficiency	NIETA	YEA	CRTF	CRIBF	Spread	NPL	CAR	LDR	NIM	OEOI
BPR KAB Bandung	79.21%	12.67%	17.27%	4.06%	6.62%	10.05%	7.21%	24.72%	97.60%	4.37%	82.30%
BPR Gunadhana Mitrasembada	74.60%	7.73%	12.42%	8.28%	0.05%	3.37%	35.14%	5.84%	90.47%	1.54%	86.33%
BPR Jelita Artha	64.87%	9.06%	11.81%	2.95%	4.72%	7.09%	18.05%	32.20%	101.47%	2.95%	70.97%
BPR Mitra Kanaka Sentosa	55.39%	10.91%	10.92%	5.67%	8.86%	8.47%	4.96%	35.83%	81.22%	4.80%	65.26%
BPR Karyajatnika Sadaya	87.97%	11.17%	12.88%	5.85%	6.20%	1.04%	11.97%	74.30%	2.22%	85.70%	
BPR Eka Bumi Artha	37.76%	3.91%	12.28%	5.49%	8.17%	4.11%	0.24%	38.94%	92.19%	2.19%	59.31%
BPR Sri Artha Lestari	51.59%	2.64%	10.15%	5.51%	6.16%	3.99%	0.03%	8.53%	66.94%	1.47%	76.82%
BPR Jawa Timur	75.36%	5.67%	10.09%	2.75%	4.36%	5.73%	0.18%	28.40%	88.45%	2.40%	80.87%

BPR KB and MKS, through the Net Interest Margin (NIM) shown to be giving a higher spread to their customer. Although a high NIM is good for business it might affect the attractiveness of the lending product.

The next part is common-size analysis, is a method of analysis in which the components of a financial statement are compared (Fabozzi and Drake, 2010) in the vertical common-size analysis, the components of a financial statement are compared to a benchmark item for that same year. This analysis compared the financial ratio of the BPR from the same quarter, while there are 8 quarters of data available for this analysis and the ratio for a single company is slightly fluctuated, there are no significant differences in the balance sheet proportion unless the strategy are changed.

When the common-size balance sheet of BPR KB is compared horizontally to other banks, the common-size balance sheet and income statement reveal a whole different story. Their balance sheet projects the financial strategy of its respective company.

BPR KB shareholder committed to provide IDR 100 billion to the company, which is paid according to the Regional Government Budget capability. The committed value is at 83% of current assets, but 65% of it are un-paid yet. The government did a right thing to postpone the equity injection to BPR KB, because BPR KB capital is still enough to handle their respective assets¹.As a matter of fact the current capital is sufficient to

¹ Note that the CAR is still at 24.72% which is very high

manage a total assets of approximately IDR 400 Billion. Nevertheless, BPR KB might need additional capital for upgrading their infrastructure.

From this analysis and benchmarking, it is clear that there are lots of rooms for improvement available in BPR KB. BPR EBA and BPR SAL have performed especially well in term of their ROE and BPR KB could benefit from the lesson learned in this analysis, whether it is the lower expenses ratio on BPR EBA, the high leverage of BPR SAL, and the diversification of revenue from BPR KS.

Since the overall company has been compared with other BPR, now it is the time to analyze deeper into the company to further exploring the business issue faced by the company

The performance of the company (i.e. Healthy) is influenced by the performance of each branch as a part of the company. Therefore an assessment of the branch performance is crucial to determining the business issue. The ratios analyzed are Cash Ratio, Non Performing Loan, Loan to Deposit Ratio, Return on Asset, and Operating Expenses to Operating Income Ratio (OEOL/BOPO), which is also known as the Operational Efficiency Ratio.

Non-performing loan is a sum of borrowed money upon which the debtor has not made his or her scheduled payments for at least 90² days. According to (Indonesia, 2004a) the tolerable number for a mediocre performing bank is in the range of 5% to 8% of the loan consequently, the lower the better. A non-performing loan higher than 8% is dangerous to the health of the bank, therefore Bank Indonesia issuing Bank Indonesia Regulation on Productive Asset Quality and Productive Asset Write-off Reserve for Rural Credit Bank PBI No. 13/26/PBI/2011 Amendment to PBI No. 8/19/PBI/2006 to prevent catastrophic failure of the rural credit bank due to non-performing asset/loan. Unfortunately after the analysis were done to the branch of BPR KB, only 40% of the branch that is performing better than mediocre.

C. Analysis of Business Situation

Non-performing loan pose serious problem in bank because it will definitely reduce the profitability of the bank. Unlike other business, loan is considered asset in a bank because the bank receive an interest for any loan they grant. Assets, Liability and

Equity is an integral part in a balance sheet, while there are 15 issues arise in this analysis the majority of this issue (9 Problem) is a balance sheet problem while some of the problem comes from income statement (2 problem) and 4 problem in the branch are because of managerial issues.

The problems in the income statement are generally the same (i.e. expenditure is too high). since the common-size analysis section of this final project explained that the expenditure is in the fixed expense (overhead) category, the rational solution is to increase the revenue by increasing the leverage factor.

The root cause that could be concluded from (Raharjo, 2012) **Error! Reference source not found.** is that the current BPR KB mediocre performance is from poor Assets and Liabilities Management. Resulting to inefficiency in the use of capital and in the operation expenses.

III. BUSINESS SOLUTION

The poor performance of the company is attributed to the performance of their respective branch. The internal cross-section analysis shows that there are no standard policies that govern the operation of the branch. Resulting un-uniform financial ratio throughout the branch. So the solution of the root cause analysis is to make a company policy guideline to govern the operational aspect of the bank's operation.

The guideline would solve the issues found in the business issue exploration and therefore solve the bank root problem. The concern of this guideline is to:

- (1) Regulate the internal financial ratio
- (2) Increase third party fund
- (3) Align the company's vision and mission to its operational practices
- (4) Reduce the amount of Non Performing Loan

Capital Adequacy Ratio is a measure of the overall capital strength compared to the risk weighted assets. The higher the ratio, the stronger the overall capital of the bank. Unfortunately, a high capital ratio also shows that the bank is unable to channel their capital funds properly. A capital ratio higher than 12% means that the bank need to increase their assets size by increasing their liability side (i.e. the third party funds).

Productive Assets Quality ratio is a measure of the the quality of the bank placement in IDR in the

² The number of days is varied according to the contract term.

forms of loans, securities, interbank placement including the commitments and contingencies at the balance sheet items. The ratio compared the loan that is substandard, doubtful or bad to the total loan. It is important that this ratio is maintained at a very low rate.

The component of the non-performing loan is guided with Bank Indonesia regulation to be lower than 5%. The top 4 BPR that is evaluated in this report has a substantially lower NPL compared to those of BPR KB. The best practice in the field of lending able to guide this ratio to be lower than 1%. Since the NPL level is already high, the best thing that BPR KB could do is to provide a restructuring program for their underperforming debtor.

Rate of return on total assets shows the earnings generated by the capital invested. Assets were formed from the combination of equity and liability, the ROA figure give the general idea on how effectively the company is converting the money it has invested into net income. Although bank indonesia consider any number larger than 1.5% is a sign of a healthy bank, BPR KB has repeatedly at least triple of the 1.5% threshold (making the threshold from Bank Indonesia obsolete). The ROA performance of BPR KB need to be improved to match other bank's performance.

Return on equity referred also as the stock holder's return on investment shows how much return is generated for the stake holder. Bank Indonesia consider an ROE in the range of 5-12.5% is sufficient for a healthy bank. The ROE of BPR KB while significantly higher than the regulation, the top 4 BPR has an even better ROE than BPR KB.

Leverage multiplier represent the value of the assets represented by the equity of the company. By this definition, it is obvious that a higher leverage multiplier indicates higher financial leverage. Seeing the current state, BPR KB could use some more leverage to boost their ROE. One thing that should be considered is the upper limit, the CAR ratio might be lower than 12% if the leverage multiplier is too high.

Operating Expenses to Operating Income shows the bank's efficiency. In this case, operational expenses hold the key. If the operational expenses is too high (the ratio is bigger than 100%) then any lending activities that the banks perform are for a loss. While Bank Indonesia only require a OEOI just under 94% to be classified as healthy. BPR KB shows that the company is capable to OEOI ratio

of under 50% in several of its branch. The rest of the red branch shown in **Error! Reference source not found.** should either increase their income or reduce their expenses.

Bank Indonesia through its circular letter and regulation require that the bank have a cash ratio of 4%, any less would make the liquidity suffer but too much liquidity would also be a cost to a bank since the cash that could be loaned, stay idly in the bank while the bank still have to pay an interest for the respective money.

A. *Alternative of Business Solution*

The bank could use a cash recycle ATM to replace cash office, because the cost of running an ATM is about IDR 4 million per month (utility) and operated 24/7, while a running cash office with 5 personnell need an initial investment of IDR 200 million and wages at IDR 6.5 million.

Cash Recycler ATM is

While the initial investment for the setup for the overall electronic banking infrastructure is greater than the current model, but the ability to run 24/7 without the need of paying overtime while at the same time lowering the operational cost.

This option would cost around USD 750,000 for a system of 30 Cash Recycler ATM compared to USD 450,000 traditional 30 Cash Office. But, in the long run (after 40 Month) the investment paid itself and for illustration purposes. If the cost of 30 ATM plus operational expenses is USD 1,398,000 within 4 years, the operational expenses of 30 Cash office during the same course of time is USD 1,458,000. This could mean an operational efficiency saving and in the end reducing OEOI and increasing the Revenue which in turn increase ROA&ROE.

While beneficial, this solution is not required at the moment since the bank has less than 10 cash office, but for the medium to long term plan the idea of having an ATM system is very attractive and the potential of increasing the operational efficiency is great. ATM system could also attract conventional bank customer to switch their account with rural bank because the system could offer higher accessibility to the customer's fund.

B. *Analysis of Business Solution*

Most of the problem existed in the company could be repaired by increasing the third party funds. The increase would brought down CAR, lowering LDR, while in the end increasing ROE. Unfortunately increasing the third party fund

is not as easy as turning the palm of hand, and require meticulous product analysis and marketing.

As previously mentioned, the bank has 2 line of product (services) which is saving and lending, to increase the third party fund the bank need to review and increase the marketing of their saving product. Judging by the current organizational structure of the bank (BPR KB) on **Error! Reference source not found.**, the company only emphasizing their attention on marketing their lending product³. While there are numerous selection of funding/saving product that BPR KB offer, there are lots of the product that offer the same feature hence the differences is only in their name.

By analyzing the products and market condition, BPR KB can do the **Product Development Strategy**, collaborated with **Product Specification Strategy** for accomodating this lacking. Product development strategy is for enhancing the benefits that BPR KB delivers to the customers by improving the existing products or developing new ones ([Perreault and McCarthy, 2006](#)). This strategy is collaborated with product specification strategy because BPR KB has to create a new product by combining the four existing products.

To introduce the products, BPR KB must have a strategy in its marketing activities. Marketing strategy is a plan of marketing action designed to achieve certain defined objectives ([Lal et al., 2005](#)). Marketing strategy process helps to ensure the marketing activities remain aligned with the BPR KB goals, maximizing the business return from BPR KB marketing efforts.

Product and service must be delivered to the target customers in the best way. BPR KB must have channels for supported the marketing activities. The value of BPR KB must be received by the customers well through communication media or channels that can be accessed easily. Today, the role of online marketing is very important for a marketing strategy. BPR KB must have an online network to support its distribution and marketing activities to strengthen the brand identity. The online marketing is to attract high-class customers, whereas to attract the middle lower customer BPR KB has to use the marketing agent for giving education and asking them to choose BPR KB

product. The promotion strategy that can be used is personal selling to draw customers directly.

IV. CONCLUSION AND IMPLEMENTATION PLAN

To increase the profitability of BPR KB, leveraging and efficiency would be the outmost important step to implement. Obviously in a bank, the best leveraging funds comes from CASA (Current Account/Saving Account) because it has the lowest cost. Thus increasing the third party fund especially Saving Account is the implementation focus of the bank.

Apart from marketing approach to increase the third party fund within the bank's assets, the bank (BPR KB) need to increase other source of revenue namely Spread and Fee based revenue. Increasing the fee based income could be done by providing various services to the customer that easing their transactional need. First BPR KB could offer a payment point for Utility, Phone, TV, Mobile Phone, etc. The bank also able to be an agent of investment product, insurance and other financial related product. This added service would be a source of fee based income for the bank.

Since BPR KB still has a high CAR (over 20%) the bank is able to increase its leverage level by increasing the third party fund, preferably savings account by doing some prized lottery. The prized lottery has been a successful tools for a bank to secure funding from a third party, since the first time BCA publish its "gebyar tahapan" until the direct prize scheme offered by OCBC NISP where the depositors would get a modern gadget without lottery if they save a certain amount of money.

Automation in many field has proven to be a sure way to increase the efficiency of an operation. This is also the case with the banking industry, most bank shift their operation to ATM by charging a fee if the depositors withdrawing money from the teller instead of ATM. This is true in most retail bank, where an ATM machine operating cost is lower than the monthly wages of a teller.

A change of legal entity could simbolize a "transformation" of the banks beareucracy and at the same time improving the bank's image. A limited liability company is also beneficial to the current owner (the regional government of Bandung Region) because it has a special legal entity trait that limit the risk of the owner of the respective legal entity to the equity being paid. So in a worst case scenario and BPR KB went

³Note that Marketing and Credit division are joined together. While this could increase the efficiency marketing of credit product, but will leave their funding product un-marketed.

bankrupt, there are no recourse to the owner outside the capital paid for the equity.

The financial ratio is the guardrail of the bank, and every employee need to understand whether the ratio reach a certain level and what to do to correct the ratio. The task of interpreting the ratio could be simplified by using some kind of dashboard software that calculate the ratio automatically from the data derived from the core banking system. The dashboard would have interpret the number and with a pre-programmed command displaying the best command to repair the ratio.

For instance whenever an NPL is occurred, the bank staff need to know the reason through KYC program and act accordingly. While of course through KYC program and 5C we could filter the possible delinquent debtor, but for a debtor that has a good character but in a financial distress there are several thing that the bank could offer. Reduce the interest Rate, Restructure the due date, Combination of the first two, if it all failed, the bank as a last resort could terminate the loan, writing it off the banking book and declare the debtor bankrupt.

When all of the idea in (Raharjo, 2012) are put in place, it would cost the bank more than IDR 1.5 billion, but excluding the investment on fixed assets then the amount the cost of marketing would be a mere IDR 354 mio. Which means that if this investment on marketing are performed, and it gather an additional IDR 8,100,686,499 of third party fund, then the bank investment is well spent. Because the third party fund it attract would create more revenue than the cost of marketing.

More detailed calculation on most optimum ratio for the bank would be interesting to be explored in the next research .Feasibility study and profitability of the ATM system on rural banking could be another interesting subject to explore. Because implementing ATM system on a rural bank has only been done in a limited scope (take BPR KS for example). The efficiency after the implementation of ATM system could be measured after the system is running and a transactional data is gathered.

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